



Memorandum

TO: HONORABLE MAYOR AND

FROM: Debra Figone

**SUBJECT: THREE-YEAR STRUCTURAL
BUDGET DEFICIT ELIMINATION
PLAN-TOP PRIORITY STRATEGIES**

DATE: May 9, 2008

RECOMMENDATION

Under the direction provided in the Mayor's March 2008 Budget Message, the City Manager's Office, along with the Redevelopment Agency, has identified a series of General Fund budget strategies which have time urgency and / or provide an immediate opportunity to implement. In some instances, additional analysis, program development or preparation for voter approval may be required. It is recommended that the City Council:

- Direct staff to proceed with further research and polling on the following measures to inform Council's consideration of asking the voters in November 2008 to:
 - Increase the Conveyance Tax by 50% and approve amendments of the current Ordinance to allow up to 40% of the parks allocation to be used for parks maintenance, and up to 40% of the non-parks allocations to be used for maintenance purposes within the specific non-parks programs funded with C&C revenues, without changing the requirement that at least 64% of the total revenues be allocated for parks purposes.
 - Authorize a City-wide Vehicle Rental Tax (either a 5% per rental or \$5 flat fee per contract depending on legal analysis) or a parking tax to apply to City and Redevelopment Agency owned and/ or other parking lots of 10%.
 - Modernize the Telephone Users portion of the Utility Users Tax and include as taxable revenues from emerging technologies.
- Direct staff to proceed with development of financing strategies with positive net present value in 2008-2009, as recommended in Proposed Budget.

RECOMMENDATION (CONT'D.)

- Direct staff to proceed with further analysis and policy development to create a rigorous asset management program, while continuing with current real estate transactions; provide a framework for this program as part of the Three-Year General Fund Structural Deficit Elimination Plan.
- Direct staff to proceed with program development and implementation of revitalized Employee Suggestion Program and Process Streamlining/Optimization Program in 2008-2009.
- Proceed with adoption of proposed 2008-2009 Fees and Charges Report; maintain current City Council cost recovery policy; conduct further analysis of current and new fees and make further recommendations in the Three-Year General Fund Structural Deficit Elimination Plan.
- Direct staff to proceed with further analysis and stakeholder outreach for a City-wide Lighting and Landscaping District including a policy analysis of non-citywide options; provide an update and status report in Three-Year General Fund Structural Deficit Elimination Plan.
- Direct staff to proceed with further analysis and stakeholder outreach to restructure the City's Business License Tax, but to not move forward any changes to that tax as a ballot measure in November of 2008.
- Drop from consideration an increase in the Sales Tax from further discussion at this time
- Drop from consideration an increase in the Transient Occupancy Tax, or a shift of existing tax proceeds to the General Fund from further discussion at this time.
- Direct staff to proceed with further analysis and stakeholder research to examine an increase in the card room tax and/or increase in number of tables allowed in card rooms.
- Direct staff to include in the 2007-2008 Year-End Budget Clean-Up Memorandum for City Council consideration and approval, any funding necessary to address immediate resource needs to support the recommendations included in this Manager's Budget Addendum.

To achieve polling and further analysis and identify strategies for a November 2008 ballot, the following schedule is recommended:

- May 16th Budget Study Session: Review of MBA and discussion of Top Priority Strategies

RECOMMENDATION (CONT'D.)

- May-June: Complete polling and analysis on the Top Priority Strategies above and begin developing ballot language
- Week of June 16th Special Study Session and/or Special City Council Meeting: review polling results and possible decisions about ballot measures
- August 5th City Council Meeting: final opportunity for City Council vote to place items on ballot

BACKGROUND

The Mayor's March 2007 Budget Message directed the City Manager to propose a balanced budget for 2007-2008 which reflected the goals and priorities of the City Council. In response to the Mayor, the Budget Director provided a memorandum outlining the full extent of the projected General Fund expenditures growth in comparison to projected revenues. The Budget Office projected that, over a five year period starting in 2008-2009, total expenditures would grow at an average rate of 4.52% while the projected growth of revenues would be 3.66%. In addition, the Budget Study Sessions in early 2007 identified and discussed the projected General Fund shortfalls for the following five years, unmet/deferred infrastructure and maintenance needs, and upcoming GASB 43/45 obligations. The February 20, 2007 City Council Priority Setting Session resulted in a decision to make solving the budget shortfall a top priority for the City Council.

In March of 2007, the City Council unanimously directed the City Manager's Office to work with the Mayor's newly formed Budget Shortfall Advisory Group (BSAG) to develop a series of strategies from which the City could eliminate the structural budget deficit. The charge to the City Manager, and her thereafter created City Manager's General Fund Structural Deficit Task Force (City Manager's Task Force), was to evaluate all options available to the City to solve the deficit within Three-Years. The City Manager's Office was also instructed to solicit and consider the feedback from a variety of community stakeholders.

The General Fund Structural Budget Deficit has been defined as the projected General Fund budget shortfall, unmet/deferred infrastructure and maintenance needs, and GASB 43/45 obligations. The most current calculations estimate the budget shortfall projections for over the next four years of \$75.1M, unmet/deferred infrastructure and maintenance needs as \$40.2M, and GASB 43/45 obligations as \$21.6M for each of the three categories and for a total shortfall of \$137M.

BACKGROUND (CONT'D.)

Beginning in October of 2007, the City Manager's Task Force began its work and retained the services of consulting firm Management Partners to conduct analysis and stakeholder outreach. Over an approximately three month process, the City Manager's Task Force, working with Management Partners, completed a report looking at a number of options for eliminating the City's General Fund structural deficit. The technical work was complimented by a series of focus groups, online surveys and a City Manager's Employee Budget Forum. A total of five focus groups with community stakeholders including community/business groups, City Labor Alliance, employees, and senior staff elicited approximately 122 new strategies and gave the groups an opportunity to share their opinions of the advantages and concerns of specific strategies. In addition, an online survey was created for both City employees and community members that asked participants a series of questions taken from the annual Community Budget Survey, for their opinions about initial strategies, and an opportunity for general comments. The employee survey elicited 2033 responses and the community survey had 656 responses.

In December of 2007, the City Manager's Task Force released a report to the BSAG group entitled, "Development of Strategies to address the City's General Fund Structural Budget Deficit." After conducting technical work and receiving input from both the community and City employees, the report examined over 300 possible strategies. The report grouped the strategies into four categories: Revenue Strategies, Service Delivery Model Changes, Expenditure Controls and Shifts, and Service Reductions. The process of identifying and implementing strategies categorized as Service Reductions was left to the existing budget process with department, City Manager, community and City Council involvement. The remaining three categories underwent a qualified/unqualified filtering process and finally, upon further analysis, a total of twenty-one Top Priority Strategies emerged as the best opportunities for the City to eliminate its structural budget deficit within Three-Years. The Top Priority Strategies are listed below:

Revenue Strategies

1. Extend Emergency Communication System Support Fee
2. Utilize Finance Strategies which have Positive Net Present Value
3. Ensure Current Fees Fully Cover All City Costs
4. Restructure Business Tax Rates to Modernize and Reflect Current Business Profile
5. Modernize Utility Users Tax and Consider Increase to Bring Into Alignment with Other Large Cities
6. Implement City-Wide Lighting and Landscaping Districts or other Proposition 218 "Property-Related" Fees
7. Levy Parcel Tax or Sales Tax for Public Safety or Other Services
8. Increase Transient Occupancy Tax to Market and Shift to General Fund

BACKGROUND (CONT'D.)

Service Delivery Model Changes

1. Formalize and Implement Rigorous Asset Management Program
2. Combine Redevelopment and City Corporate Support Functions and Shift Economic Development Costs to Maximum Extent Possible
3. Revise Competition Policy, Implement Managed Competition for Service Delivery, and/or Optimize Work Processes
4. Increase Utilization of Civilian Positions in Police and Fire
5. Eliminate Binding Interest Arbitration
6. Modify Minimum Fire Staffing Policies where Appropriate Based on Fire Strategic Plan
7. Implement an Employee Suggestion and Process Streamlining Program

Expenditure Controls and Shifts

1. Shift Healthy Neighborhood Venture Fund Funding to General Fund
2. Reduce Workers' Compensation, Disability, and Overtime Costs
3. Shift Construction and Conveyance Tax Funding from Capital Projects to Operating and Maintenance Costs
4. Reduce the Rate of Increase in Employee Salary and Benefit Costs
 - a. Increase Time to Reach Maximum Compensation
 - b. Reduce Entry-Level Compensation Benchmarks for Positions for which the City receives Many, Qualified Applicants
 - c. Implement Health Care Plan Modifications
 - d. Implement Sick Leave Payment Upon Retirement Program Modifications
5. Change Prevailing Wage Applications: Eliminate Service Contracts

Service Reductions

Reduce/Eliminate City Services to Funding Capacity

The report also recommended a series of Budget Principles for City Council adoption, which, if adopted and followed, were recommended as means to avoid future structural budget shortfalls. In January of 2008, the report's findings were presented to the BSAG for its consideration and possible recommendation to the City Council. On January 30, 2008 the BSAG group voted to forward a series of recommendations to the City Council for the elimination of the structural budget deficit, for the 2008-2009 budget specifically and the budget process on the whole. Included in the recommendations was a structure for the City Council to address the budget deficit over Three-Years by allocating one-third of the amount the budget deficit in each of three areas: (1) Revenue Increases (including economic development) (2) Service Reductions (3) Cost Savings.

The City Council when reviewing the BSAG recommendations directed the City Manager and Redevelopment Agency Executive Director to further the budget deficit elimination efforts by providing City Council with a series of recommendations in May 2008 for City Council to consider for immediate action and then for the completion of a Three-Year Structural Deficit Elimination Plan by November 2008. In addition, the Mayor's March Budget Memo provided

BACKGROUND (CONT'D.)

for the Council to appoint a Stakeholder Group to advise the City Manager and Redevelopment Agency Executive Director about advantages and concerns regarding each of the identified strategies and to suggest additional strategies to eliminate the structural budget deficit.

Of the twenty-one strategies identified as Top Priorities in the December 2007 report, ten strategies fall into the category of “Urgent” because the City has the ability to implement the strategy in the short-term without significant additional analysis, the strategy does not require meeting and conferring with employee bargaining groups, there is consensus that the strategy should be implemented or, for those strategies that require voter approval, the City may want to consider placing a measure on the ballot in November 2008. The criterion applied to rank the strategies included fiscal payoff, length of time to accomplish the strategy, ease of implementation, stakeholder consensus, political complexity and whether voter approval is required.

Current Project

An internal team (the Core Team), convened by the City Manager in April 2008, is tasked with developing a Three-Year Structural Budget Deficit Elimination Plan to be presented to the City Council in November 2008. The Core Team is organized into Sub-Teams around budget deficit elimination strategies. Each Sub-Team has a City staff member as team leader with team members from staff, Management Partners and the City Attorney’s office.

The first task of the Core Team was to analyze Strategies that have timing urgency or an opportunity for immediate implementation. The Core Team is also providing assistance to the Stakeholder Group appointed by the City Council in April. Analysis of the initial ten strategies is included for consideration by the Council as part of the May budget discussions as directed in the March Budget Message.

The Core Team will continue its work with the Stakeholder Group through September 2008 to complete the analysis of other strategies identified in the January 2008 report that could potentially address the structural budget deficit over the next Three-Years. Additional ideas, identified through the Stakeholder meetings will be included in the Three-Year General Fund Structural Deficit Elimination Plan scheduled for presentation and discussion in November 2008.

The City Council has approved a six-month stakeholder group budget outreach process consisting of four steps:

1. Top Priority Strategies: Discuss *Advantages* and *Concerns* for Top Strategies identified by the City Manager that should be brought forward to the City Council in May for consideration due to timing urgency and/or an immediate opportunity to implement.
2. Other Strategies: The Stakeholder Group will identify *Advantages* and *Concerns* for other strategies by September.
3. Exploring Additional Ideas: The Stakeholder Group will develop alternatives and options for consideration in the Three-Year General Fund Structural Deficit Elimination Plan.

BACKGROUND (CONT'D.)

4. Feedback: The City Manager and Redevelopment Agency Executive Director will include a summary of Stakeholder Group's *Advantages* and *Concerns* as part of the Three-Year General Fund Structural Deficit Elimination Plan to be released in November.

City staff has been charged with providing technical information on each strategy to the Stakeholder Group and obtaining any additional information needed on each strategy beyond what is available at the stakeholders meetings. The role of the Stakeholder Group is to discuss the advantages and concerns of each strategy. The public is invited to all stakeholders meetings and is invited to offer comments at the meetings.

The Stakeholder Group was appointed by Council on April 8, 2008. Councilmember Pete Constant chairs a group of twenty-three stakeholder representatives, including business, labor, city employees, tax payers, non-profits and neighborhoods. The Stakeholder group met three times in April and May and discussed advantages and concerns of the strategies discussed in this document.

The structural budget deficit is a major community concern. Concurrent with the City's process of identifying options to close the deficit, a community budget working group, San Jose Excels!, formed to develop recommended strategies for consideration by the City. A number of their recommendations are similar to those developed by City staff and Management Partners. There is opportunity for consideration of additional proposals, such as those brought forward by members of the Stakeholder Group, San Jose Excels! neighborhood organizations, non-profits and other groups during the stakeholders process over the next five months.

ANALYSIS OF TOP PRIORITY STRATEGIES

In the following discussion the work accomplished by the Core Team during April and May with respect to Top Priority Strategies which provides the basis for the recommendations in this MBA is reviewed. The following Top Priority Strategies are discussed:

- Increase Conveyance Tax and/or Shift Construction Tax and Conveyance Tax funding from Capital Projects to Operations & Maintenance (O&M)
- Increase revenues from visitors who benefit from General Fund services, by: (a) increasing Transient Occupancy Tax (TOT) to market and shift to General Fund, (b) establish a parking tax on City and RDA owned lots, or (c) establish a vehicle rental tax
- Modernize Utility Users Tax (UUT) and Consider Increase to Bring Into Alignment with Other Large Cities
- Utilize Financial Strategies that have Positive Net Present Value

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

- Implement an Asset Management Program
- Implement an Employee Suggestion and Process Streamlining Program
- Ensure all fees are full cost recovery
- Implement Citywide Lighting and Landscaping District
- Restructure Business Tax to Modernize and Reflect Current Business Profile
- Increase Sales Tax to Provide Increased General Fund Revenues

Input from the Stakeholder Group on each of these strategies has been provided solicited at meetings held on April 21, April 28 and May 5. A synopsis of each of these meetings is attached to this MBA. Stakeholder Group input has helped to shape the recommendations provided here and will continue to inform the process of developing the General Fund Structural Deficit Elimination Plan. It is important to keep in mind that further stakeholder input along with additional work by staff will be taking place over the next five months as part of bringing an overall strategic plan to the City Council in November 2008.

Strategy: Increase Conveyance Tax and/or Shift Construction Tax and Conveyance Tax funding from Capital Projects to Operations & Maintenance (O&M)

The Construction and Conveyance Taxes are a significant source of revenue for the City. The Construction Tax is imposed on the construction of residential, commercial and industrial buildings while the Conveyance Tax (often referred to as a Real Property Transfer Tax by other jurisdictions), is associated with the transfer of real property. The two taxes are estimated to raise approximately \$23 million in 2008-2009, 98% of which is derived from the Conveyance Tax. Historically, revenue from the two taxes has varied over time. The current projections for 2009-2010 are 45% less than the peak in 2005-2006. The current Conveyance tax rate is \$3.30 per \$1,000 of the value of the property transferred. Since only 2% of the revenue is derived from the Construction Tax and the remaining 98% is derived from the Conveyance Tax, this strategy only focuses on the Conveyance Tax.

Although the taxes are usually general taxes in most jurisdictions, the City's taxes are dedicated to specific purposes. Specifically by Ordinance, at least 64% of the revenues must be allocated for parks purposes and the remainder, up to 36%, may be allocated for a number of purposes including library facilities, equipment and collections, fire facilities and equipment, parks and public works service yards, communication facilities and equipment, or other capital projects as determined by the City Council. Of the amount allocated for parks and parks-related service yards, up to 15% may be transferred to the General Fund for park maintenance.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

When revenues per capita are examined, the City of San Jose is well below its large city peers who have an average of \$59.60 per capita with the City's revenues per capita being \$29.03. The City's revenues are slightly higher than other local jurisdictions that have an average of \$20.78. Several large charter cities in the Bay Area have a conveyance tax rate significantly higher than in San Jose.

The allocation of revenue is another area where the City varies from its large city peers and local jurisdictions. Of the fourteen cities examined, only the City of Mountain View, like San José, restricts the use of revenues. The other thirteen cities place all revenues into the General Fund for general purposes.

It should be noted that the City's current allocation does provide a dedicated revenue stream for capital infrastructure such as parks, libraries and fire stations. This strategy continues to provide the City with a funding source that helps address its infrastructure backlog, which is also one of the Council's top five priorities, and provides funding for other critical needs such as fire fighting and communications equipment and library materials.

The proposed strategy examined a series of options while taking the above factors into consideration. These options included various shifts in revenues from dedicated programs and services to operations and maintenance in the General Fund as well as an increase in the Conveyance Tax. All options, to varying degrees, help reduce the General Fund structural budget deficit. Option D would do so to an unquantifiable extent in that it would simply provide flexibility in how General Fund dollars could be spent.

- A. Increase Conveyance Tax by 50%: shift up to 40% of parks allocation to park maintenance; maintain current allocation of revenues
- B. No increase in Conveyance Tax: shift up to 30% of parks allocation to park maintenance
- C. No increase in Conveyance Tax: shift all revenues to General Fund
- D. No increase in Conveyance Tax: maintain current allocations; reprioritize the 36% allocated for the non-parks purposes to other capital uses

The potential fiscal impact of each option is currently estimated (based on annual projected collection levels) as follows:

- A. Increases overall revenues by \$11.3M: increases Park Maintenance by approximately \$6.6M; additional \$4.7M for other uses
- B. Increases Parks Maintenance approximately \$2.2M; decreases Parks Capital by approximately \$2.2M
- C. Increases General Fund revenues by \$20.8M, corresponding decreases in funding for programs funded by revenues
- D. No changes in funding amounts; shifts funds within the 36% allocation

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

A series of objectives was established to help evaluate the options. The objectives take the entire structural budget deficit into consideration including the reduction of the deferred maintenance and infrastructure backlog along with increasing General Fund revenues.

1. Reduce the City's deferred maintenance and infrastructure backlog
2. Decrease the City's General Fund Structural Budget Deficit
3. Provide more flexibility to include operating and maintenance expenditures
4. Ensure available funding to address ongoing infrastructure needs

Of the four options, only Option A meets all four objectives. Option B meets Objectives 2 and 3; Option C meets Objective 2 and Option D meets Objective 1.

Each option has varying approval requirements to increase the tax or change allocations. Option A to raise the rate and shift some funds to maintenance would require two-thirds voter approval. Option B with no overall increase but a shift in some funds would also require a two-thirds voter approval. Option C to shifting all revenues to the General Fund requires a simple majority voter approval. And finally, Option D, shifting the non-Parks allocation requires approval from the City Council.

Depending on the option chosen to go forward, the timeline would range between three months for City Council action of Option D to six months for voter approval of the remaining options if one of them were to be placed on the November 2008 ballot. For all ballot measures, specific ballot language would need to be developed and then polled with likely voters. The final step to place an Option on the November 2008 ballot would be City Council approval, which must occur no later than the City Council meeting scheduled for August 5, 2008.

Strategy: Increase revenues from visitors who benefit from General Fund services, by: (a) increasing Transient Occupancy Tax (TOT) to market and shift to General Fund, (b) establish a parking tax on City and RDA owned lots, or (c) establish a vehicle rental tax

The purpose of a Transit Occupancy Tax (TOT) is to recover costs associated with providing city services to visitors in the form of what is often called a "Bed Tax." Visitors who spend at least one night and no more than 30 nights are charged a tax to defray the costs of general services utilized while in a city.

Currently the TOT in the City of San José is below market to its large City peers. The current rate is 10% versus 12.5% average of the ten largest cities plus Fremont in the State of California. Local jurisdictions in the Silicon Valley average 9.13% in their TOT rates. When revenue per capita is examined the City is below market to both its state-wide peers and local jurisdictions. When examining the TOT, it was also found that the City has directed a portion of its TOT revenues for specific funds beyond the General Fund. The total TOT consists of a special tax and a general tax. The breakdown of revenues to the General Fund is 40% while the remaining 60% is dedicated to support the Convention and Visitor's Bureau, grants for fine arts, and the

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

operating subsidy for convention center facility operations. Again, when examining the large city peers and local jurisdictions, the City is below its large City peers and well below local jurisdictions. Large city peers, on average direct a little over 75% of its TOT revenue directly to General Fund and local jurisdictions direct 95% to General Funds while the City directs only 40%.

Although the Management Partners report suggested exploring both a raise in the City's TOT rate and shift all revenues directly into the General Fund, it should be noted that the City and Redevelopment Agency have been engaged in ongoing discussions with local hotel owners to establish a "Hotel Taxing District" supporting the renovation and expansion of the convention center. The current concept being discussed, that has been presented to the City Council, would have the hotels collecting an additional 4% or more on hotel room rate (calculated in a similar fashion to TOT) and these revenues used to finance the renovation and expansion of the existing convention center.

It was the recommendation of the Core Team to consider other options to defray visitors' costs in light of the progressing negotiations for the "Hotel Taxing District." The other strategy options considered were a new parking tax for users of City and RDA owned parking lots, a parking tax for users of City and RDA owned lots plus private lots and/or a vehicle rental tax for all vehicle rented within City limits. At present, the City does not have a tax levied against either parking or rental vehicles.

When surveyed, the majority of large California cities with major airports have parking lot taxes. The cities surrounding San Francisco International Airport have either parking taxes or special assessments for parking in the rate of 8% and the Cities of Oakland and Los Angeles' rate is 10%. Other cities with large visitor bases but without nearby airports also have parking taxes. The San Francisco has a parking tax rate of 25%. In all example cities with a parking tax, the tax applies to both City-owned and privately owned parking lots. In addition, San Francisco has in its municipal code the ability to levy a tax on the rental of vehicles within the city limits but it is apparently not enforced. The vehicle rental tax may face complications for state law preemptions and further legal research will be necessary to full illuminate this question.

Because the City's General Fund receives relatively limited funding relative to other large California cities for taxes imposed on transient, or visitor related uses a series of options beyond raising the TOT rate were considered. The following outlines the options under consideration and the associated potential fiscal impacts. All figures would be annual revenue directed exclusively to the General Fund:

1. Impose a 10% parking tax on users of City and RDA owned parking lots: approximately \$5.1M
2. Impose a 10% parking tax on users of all parking lots, public and private: approximately \$9.0M

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

3. Impose a 5% vehicle rental tax on all vehicles rented in the City: approximately \$7.5M
4. Impose a \$5 flat fee per vehicle rental contract in the City: approximately \$4.7M

The City and RDA parking lots include airport parking lots, San Jose Arena lots, Regional Parks and other lots throughout the City. It should be noted that several RDA lots are temporary with long term development planned and that Arena estimated are based on projected and not actual revenues realized. The private lot revenues are based upon estimated gross revenues of downtown lots and Diridon/Arena lots. Further analysis would be required to establish a more accurate estimate of proposed tax revenues. As previously stated the Parking Tax and Vehicle Rental Tax require more analysis to address legal feasibility.

For all four options, majority voter approval would be required. To place the issue on the ballot in November of 2008, ballot language would need to be developed in the coming months and likely voters polled. If Option 2, 3, or 4 moves forward, outreach to affected stakeholders would be required before a measure is placed on the ballot in early August.

Strategy: Modernize Utility Users Tax (UUT) and Consider Increase to Bring Into Alignment with Other Large Cities

The UUT is a general tax imposed on utility bills, typically as a straight percentage of the utility costs. The last major overhaul in San José's UUT dates to the 1980s when the major utilities and the League of California Cities negotiated a model ordinance. San José's ordinance is based on that model ordinance. Of course, much has changed since the 1980s especially with respect to telecommunications; wireless technology and the internet revolution are the two main drivers of changes in the telecommunications "utility."

Another issue impacting the UUT is the fact that Proposition 218 has been interpreted to require voter approval of any methodology change in calculating the tax. With the service providers constantly changing the way services are provided, tax administration methodologies also have to evolve or the tax revenues erode. Adding to the complexity are federal interpretations altering the application of the Federal Excise Tax on telephones.

As a result of these changes, over 100 cities in California that rely on an UUT including telecommunications (such as San José) have an intense interest in maintaining the integrity of their UUT. Thus, the state is currently undergoing another round of changes to city utility taxes that is being driven mainly by litigation by the telecommunications company Verizon, which wants to reduce the scope of utility taxes as applied to its services. Therefore, aside from the issue of closing the structural deficit, San José may need to look for an opportunity to seek voter approval of an updated ordinance for the UUT that reflects the realities of the modern telecommunications industry.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

Currently San José has a UUT rate of 5%, which is lower than several peer cities. San Francisco, Sacramento and Oakland all have UUTs at 7.5% and Los Angeles has a UUT at 10%. Oakland has special provisions in place; the UUT is frozen at 5% for persons identified as being low income. San José collects UUT revenues of \$77 per capita, which is considerably lower than its peers. Los Angeles collects \$149, Sacramento collects \$119 and Oakland collects \$107.

In the last four elections, 26 California cities asked their voters to add, modify or continue their existing UUT. The measures endeavored to respond to changes in telecommunications technology, billing practices and federal law, by modernizing their UUT ordinances to clearly and lawfully cover new approaches to selling communications and information services.

Nine of the successful measures modernized the UUT without any reduction in the tax rate. Thirteen of the successful measures reduced rates on existing city UUT on telecommunications. The City of South Pasadena was the only agency to successfully increase its UUT rate by 3% (to 8%) for a five-year period and accompanied this measure with an advisory measure requesting voter opinion regarding dedicating the tax to infrastructure (65%) and employee compensation (35%). The South Pasadena successful UUT increase applies to telecommunications, electric, gas, cable TV, and water utilities. The City of Menlo Park successfully implemented a new UUT of 3.5% on electric, gas and water and a 2.5% rate on telecommunications. Two measures failed, including a new tax on gas and electric in Fremont.

Option A: Increase All UUT Rates

San José collected \$7.1M in UUT revenues in 2006-2007. Revenues for 2008-2009 are estimated to be \$83.4M. San José could realize increased revenues of \$4.2 M for every 0.25% increase in its UUT rate. Increasing the tax rate to the state average for cities with a utility tax (5.5%) would represent an increase of \$8.4M. Raising the tax to the average for larger cities (7.5%) would yield approximately \$41.9M based on the existing tax structure. Increasing the UUT would require outreach to residents and business groups and it is likely a measure could not be placed on the ballot until June or November 2010. A majority vote of the Council is required to place the measure on the ballot and a majority electoral vote is required to increase the UUT.

Option B: Maintain Current Tax Rate and Modernize Telephone Users Tax

One reason for the disparity between per capita revenues collected in San José and larger peer cities is that the San José UUT is not as comprehensive as most other large city UUT ordinances, as it does not include interstate/international telephone services or cable television services. If the City were to modernize its UUT, it could probably broaden the application to cover emerging service approaches in telecommunications and potentially other bundled communications services. This has been the recent trend in California.

It is likely that older technologies (e.g., landlines) will continue to be replaced by newer technologies. Modernizing the telephone utility users tax language to include the City's intent to tax emerging technology as it develops may offset some of the revenues that would otherwise be lost as a result of decreasing consumer costs. Failure to tax newer technologies would not only

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

result in substantial decline in revenue, but would also create an inequitable situation where those who can afford newer technologies are not taxed, while those paying to obtain the same type of services through older technologies continue to be taxed. The intent is to have an equitable tax that applies to all users of telephone services, whether traditional landline, wireless or broadband telephone service, to the extent permitted by state and federal law.

To implement this alternative, additional funds may be needed for staff to secure an expert in telecommunication services to help assist with the ballot measure and ordinance to ensure that the ballot language and ordinance are as comprehensive as possible to be able to capture emerging technologies. Maintaining the current UUT rate and modernizing the telephone users tax is estimated to generate an additional \$1-\$2M annually to the General Fund. Future potential revenue could be realized as new technologies emerge. A majority vote of the Council is required to place the measure on the ballot and a majority electoral vote is required for implementation.

Strategy: Utilize Financial Strategies that have Positive Net Present Value

Option A: Annual Prepayment of City's Pension Payment Obligations

Currently, the City makes employer pension contributions with the biweekly payroll. Under the suggested approach, the City would instead pay to the Police and Fire Department Retirement Plan and the Federated City Employees' Retirement System (the "Retirement Plans") its full annual employer contribution near the beginning of the fiscal year. Staff's preliminary analysis indicates that it would be beneficial to both the City and the Retirement Plans if the City were to make annual prepayments of its employer contributions to the Retirement Plans in lieu of biweekly contributions. The Retirement Plans would each give the City a discount on the prepayment based on the assumption that the Retirement Plans will earn more during the coming year by having 100% of the City's contributions available for investment at the beginning of the year. The annual savings to the City is estimated up to \$1M. The benefit would primarily be realized in the form of a lower unfunded accrued actuarial liability ("UAAL") and lower total annual employer contributions.

Although the Retirement Plans do not currently offer a discount to the City for prepaying retirement contributions annually in advance rather than biweekly, other public retirement systems have established policies permitting annual prepayment at a discount. This includes public retirement systems such as the California Public Employees' Retirement System (CalPERS) and the Los Angeles City Employees' Retirement System.

The City has assembled a team of interdepartmental staff and consultants (the "Team") to proceed from the preliminary analysis and begin developing a prepayment proposal. The Team consists of staff from Retirement Services, Finance, the City Attorney's Office, Human Resources, the Office of Employee Relations, the Boards' respective actuaries, and the City's financial advisor. Both Retirement Boards have directed their respective actuaries to develop an actuarial analysis of the discounted annual contribution. Both actuaries provided their respective

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

report to the Boards at the Boards' May meetings. Updates to their respective reports will be presented at the June meetings of both Boards. Proposed amendments to the Municipal Code will be presented to the Retirement Boards at their June meetings in order to authorize the City's prepayment of its annual employer contribution. The Council is expected to consider these amendments to the Municipal Code in late June. The amendments are anticipated to be effective as of late July. Prepayments would not commence until after the amendments become effective. The 2008-2009 Proposed Operating Budget recommends proceeding with this strategy.

Option B: City to Issue Pension Obligation Bonds

Preliminary analysis of the issuance of Pension Obligation Bonds (POBs) indicates that it would be beneficial to both the City and the Federated City Employees' Retirement System (the "Federated Plan") if the City issues POBs and deposits proceeds with the Federated Plan which has a higher earnings rate than the estimated interest rate that the City would pay on the POBs. The combination of restrictions on investment options for a city's idle funds and the potential higher returns available on monies invested by pension plans has spurred the growth in the use of POBs. Since 2002 at least 42 California cities have issued POBs in amounts ranging from \$4 million to \$20M. During the same time period, 18 California counties have also issued POBs in amounts ranging from \$7M to \$505M.

POBs can be risky if they are relied on to fund a relatively large share of pension obligations. However, in San José, the Police and Fire Plan is almost fully funded and the Federated Plan is 82.7% funded for the pension benefits provided by the respective plans. This strategy proposes that the City issue approximately \$150M in POBs to raise the actuarial funding level of the Federated Plan for the pension benefit to approximately 90%. The estimated higher earnings on funds invested in the Federated Plan are projected to translate into lower employer retirement contribution rates for the City. Based on current market conditions, it is anticipated that a POBs issuance could generate annual net savings ranging from \$1.5M in the first year, escalating to \$4.9M annually per year by year 10, and then continuing at that level throughout the remaining 17 years of the 27-year bond repayment schedule. The net savings would be realized by the City due to the difference between lower contributions to the Federated Retirement Plan and debt service payments on the POBs.

Costs for implementing the proposal includes financial advisory fees and outside legal counsel, which are reimbursable from bond proceeds, and additional staffing beginning in 2008-2009. Assuming the bonds are issued for this strategy, most of the up-front, onetime costs are subject to reimbursement from the POBs proceeds.

Implementation of this strategy requires approval by the Federated Retirement Board for receipt of the bond proceeds, Council approval of the bond issuance and a court validation process. Most importantly, the Federated Retirement Board must also approve revised contribution rates based on a higher funded accrued actuarial liability, in order to actually lower contributions from the City to the Federated Plan.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

Strategy: Implement an Asset Management Program

A "rigorous Asset Management Program" can be defined as a systematic and ongoing effort to (a) review and evaluate the cost-effectiveness of current or planned uses of City-owned property, (b) determine when potential opportunity costs or competing service priorities justify consideration of alternative uses, and (c) when appropriate, sell or lease property to another party. Undertaking such a program would require a significant effort by the City, since successful implementation requires extensive outreach, transactional resources, and an approval framework that is designed to support timely decision making among potentially conflicting values and priorities.

The City currently purchases, sells and leases its real property assets on a transactional basis consistent with the City's Charter and Municipal Code, State Law and Council Policy. However the City does not manage its real property holdings as an asset with an eye to raising ongoing revenue. The City does not have a program to manage these assets from a revenue generation perspective and this has resulted in an accumulation of property over time as well as inconsistent criteria used for leasing property and operating city assets. This presents the City with an excellent opportunity to better manage its assets and address the Structural Budget Deficit through implementation of a rigorous asset management program. In order to change this situation the City Council will need to consider and adopt a policy that makes the generation of current and one-time revenue generation from City property an objective to be considered (along with other objectives) in the management of real property assets.

Presently the City owns approximately 1080 parcels. Approximately half of these properties are used to directly support City services such as the City Hall, libraries, parks and police/fire stations. The remaining parcels fall into several categories of property:

- Vacant and/or underutilized
- Operated by non-city entities
- Leased to non-city entities
- Miscellaneous and unidentified parcels

Research of other Cities' asset management programs, has found an array of property related policies and asset management programs:

- San Diego, C.A. implemented policies to address below-market rate lease and disposal of unneeded property, and projected \$100M in revenue for its five year budget.
- Charlotte, N.C. has helped bridge their budget gap through implementation of a program, review of asset use entities by its Planning Commission before Council approval. They have reported \$15M from 125 transactions.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

- Seattle formally reviews its real property assets through its Real Estate Oversight Committee. The program has been in place since 1998 and generates approximately \$500,000 annually.

Research indicates that successful Asset Management Programs are those where Council sets policy based on community goals and priorities. These policies include criterion for leasing property, operating facilities, or deeming property surplus. In addition, highly-defined program goals and performance measures are typically established to ensure program consistency.

Implementation of an asset management program is a major undertaking. Key elements of a successful asset management programs are likely to include:

1. *Program and Performance Goals* - As a critical element of accountability, the Asset Management Program would be guided by principles that set benchmarks that will assist in identifying assets that no longer contribute to established goals. Performance measures would also be established to monitor actual asset disposal performance with expected results.
2. *Formalized Reporting* - Review of existing properties and their use would be formalized. This step would bring forth information related to the use of City assets and provide an opportunity to evaluate alternative uses. This step may not necessarily involve a decision to discontinue an operation or sell a property. This step could simply begin an evaluation of options. An appropriate Commission, Council Committee, or the full Council could provide a venue for formal initiation.
3. *Broadened Evaluation of Potential Use* - Outreach to prospective partners/buyers would take the form of a Request for Qualifications/Proposals, public bid, or other process. Based on interest from prospective partners/buyers, staff would evaluate alternatives and recommend disposition such as continuing current uses, lease, or sale. Sensitive or complex transactions would involve additional stakeholder outreach to review staff recommendations.

As previously stated, undertaking a comprehensive and rigorous approach to asset management will require development and approval of a policy framework as well as resource allocation to continue program development and implementation. To proceed toward this strategy, the following three steps are recommended:

1. SHORT TERM PRIORITY SURPLUSING OF PROPERTY

In the short term, staff would evaluate properties that are strong candidates to be surplus consistent with existing policy. These include properties that are vacant and/or have been underutilized for an extended period of time. Staff would begin immediately and may be able to generate revenue in the second half of 2008-2009. It should be noted that several properties have already been identified for potential sale, and are at varying points in the surplus process.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

- a. Resources to implement - included in the proposed budget
- b. Estimated Revenue - \$500,000 - \$1M in 2008-2009

2. DEVELOP ASSET MANAGEMENT PROGRAM

There are two major steps that can occur concurrently. First, staff recommends adopting guidelines for consistent asset management based on City Council policy and priorities. The second step, would be to develop a comprehensive inventory of the City's real property assets. This inventory will allow the City to have a complete picture of its assets and thus manage them more efficiently and effectively. To complete the inventory the City will likely need to invest resources either in permanent staff, specialized consultants or some blend of the two. Estimated revenue would be determined by the policy and program goals.

3. PROCEED WITH AN EVALUATION OF EXISTING MAJOR PROPERTIES AND OPERATIONS

The purpose of this work is for staff to bring forth recommendations to initiate the analysis needed to have a policy discussion regarding major City owned properties and operations and for potential alternative uses or sale of these assets. These could include:

- a. Golf Courses – a Citywide operational and financial review has recently been completed.
- b. Mexican Heritage Plaza - a solicitation for a nonprofit operator is currently being developed.
- c. Hayes Mansion – Periodic financial reports currently review debt service, revenue generation, facility assessment and maintenance needs. The property continues to require City subsidy.
- d. Old City Hall – a cost analysis to renovate and reoccupy is currently under way. This analysis will support a decision whether to renovate, engage a private partner, or pursue sale of portions of the property.
- e. San Jose Water Utility – This utility serves a small segment of the community. Recent legal determinations have prevented the City from operating and managing this asset such that it makes a significant return on investment for the City General Fund. Given these restrictions an analysis may show the City would be better off financially to transfer ownership.
- f. Singleton and Story Road Landfills - Staff has recently received private sector interest in brownfield development of the City's two closed landfills at Singleton (Capitol Expressway) and Story Road at Remillard Court. Given that landfill monitoring and other infrastructure at these sites is aging and will need additional investment in the near future, timing may be appropriate to investigate adaptive reuse options.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

The authority to enact changes in the status of these properties resides with the City Council. It is expected that policy development could take about six months to complete. After the policy is developed, creation of measurable objectives and a work plan as well as initiation of the work plan's identified tasks will be completed within 12 to 18 months. During the program development, a full inventory of the City's assets would be required. During the 18 to 24 months outlined above, the City would continue to process transactions with emphasis on transactions that generate revenue. Staff would also attempt to ramp up this program on an aggressive schedule, concurrently completing as much of the start-up work as possible and prioritizing efforts toward those assets which have the most potential to generate significant ongoing or one-time revenues.

Strategy: Implement a Revamped Employee Suggestion and Process Streamlining / Optimization Program

The Employee Survey conducted in conjunction with City Manager's Structural Budget Deficit Elimination Plan in the Fall of 2007 brought to light City employees' willingness to provide strong ideas to create a more efficient working environment. The survey elicited approximately 950 comments which were categorized and qualified/disqualified for inclusion in the report. The quality and quantity of the suggestions were impressive and evoked the idea of revitalizing a dormant employee suggestion program. Such a program would focus on areas of process streamlining and efficiencies identified by the unique insight City employees have about how the City conducts its business.

Employee Suggestion Programs (ESPs) were pioneered by the private sector and have had significant success for industries with a great number of front line employees. One example is American Airlines which began its program to reduce costs in the early 1980's. Employees would be financially rewarded for cutting costs by receiving a percentage of the money saved; 8-10% of cost savings realized with a cap of \$25,000 per idea. American Airlines reported the company saved \$50 million annually over the last twenty years.

The concept of ESPs has spread to government with more limited success. The State of Oregon's program is also based on percentage cash rewards for employees with ideas that produce results. The State rewards 10% of monies saved with a cap of \$5,000 per idea. Over a Three-Year period, more than 130 ideas have been submitted and 17 accepted with a savings of approximately \$1.3 million for the State. The department which realizes the savings retains the funds saved and pays the employee reward. The program is administered by dedicated staff with the Human Resources Department and all full-time employees are eligible to participate.

The City of Phoenix's ESP program has existed since 1991. In a recent revision to its program policy, Phoenix now allows employees to submit suggestions that pertain to their departments and individual work responsibilities. The City recognizes that employees who perform the work are best suited to identify streamlining ideas. Employee ideas can be submitted online and are acknowledged within three days. Decision about cost savings and rewards are provided to the

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

employee within 60 days. The department which will be affected by an idea has the opportunity to evaluate its implications and potential fiscal impact. On the whole, the program is administered with the Human Resources Department and currently includes 25% of an HR Coordinator's and 60% of an Administrative Clerk's time and duties. The program also budgets approximately \$4,000 a year to reward employees who provide ideas with intangible results. Since its inception, the program has saved the City approximately \$1.6 million.

The City of San Jose established a Suggestion Award Program in 1965, but it has been dormant for several years. An Art & Practice of Leadership (APL), the City's professional development program, class re-examined the Suggestion Award Program as part of its project requirements. The result is a proposed program which can revitalize the current program in three key ways. 1. Expedite and simplify the awards process; 2. Expand eligibility criteria; and 3. Enhance outreach activities. The specifics of this program are still being developed but would include expanded eligibility criteria, quicker and easier feedback on ideas submitted and improved rewards for successful ideas.

In the best-implemented and managed ESPs, the program's administrative costs, including rewards, can cover its expenses through realized cost savings. Although difficult to quantify, there is potential for the program to provide real cost savings to the City and aid the structural budget deficit. In addition, the program will empower City employees to be active participants in eliminating the deficit and streamlining the way they do their work. The City has experienced an extended period of reductions which employees have responded to with hard work and dedication. A revitalized ESP can help sustain employee morale during difficult times.

The authority to enact lies in the City Council. It is estimated that up to six months would be required to develop program revisions for approval by Council and then another six months to fully implement the program. Research has indicated that successful on-going programs also include dedicated staff and budget, which includes outreach and intangible rewards expenses on an annual basis. At present, the City has an Innovation Fund with a balance of \$100,000 and yearly annual budget for the current employee suggestion program of \$25,000. The Innovation Fund could serve as start-up funding assistance.

Another separate, but related part of this program will be a process streamlining or optimization program for City business processes. Many times employees have identified City business processes which consume an inordinate amount of time and / or return relatively little value. However beyond the identification of such business processes employees may not know how they should best be reformed. This often requires the dedicated services of a staff or consultant team that can research best practices, develop process maps and generally redesign the work effort to be more efficient. Starting in 2008-2009 the City Manager will select some City business processes for redesign or optimization and fund one-time costs associated with the process improvement efforts.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

Strategy: Ensure all fees are full cost recovery

Cities have the ability to charge fees for City services to the extent permitted by law. In most cases, fees may not exceed the City's actual cost of providing the particular service.

Historically, the City has categorized user fees into two categories: Category I full cost recovery and Category II less than or more than full cost recovery. The policy decisions to define two categories of fees reflect City Council priorities to subsidize the costs of particular services to residents for the community. In most instances subsidized services provided are within departments such as Parks, Recreation, and Neighborhood Services and programs which assist children and/or senior citizens.

The City produces a Fees and Charges Report as a separate document during each budget cycle. The Report outlines fees according to cost recovery category and where City services fall within the spectrum. The City takes this opportunity to evaluate its fees in order to determine whether fees which are limited to cost recovery should be increased or decreased. Similarly, the City also evaluates whether fees for services which have been designated as below or above cost recovery require adjustment.

Further examination of the particular fees in the Fees and Charges Report and the fee schedule was initiated. Specifically, Category I & II fees were studied, new fees were researched, and the concept of fee development to manage demand for services was developed. There are a series of new and existing fees which either have potential for immediate fiscal impact for the City or should begin the process of implementation because the fees have greater potential fiscal impact in the future. In addition, other fees were identified for more research but the departments which would be affected by new or raised fees were not part of the current discussion. As part of the Three-Year Structural Budget Deficit Elimination Plan, the fees will be revisited to include all departments and to conduct full fiscal analysis, with respect to the ability to raise existing fees to fully cover costs and to initiate collection of fees for user based services when warranted.

Because the current Top Priority Strategy is meant to identify immediate opportunities for enhanced revenue, the research associated with fees focused on the ability to raise fees already in place, or for fee initiatives already underway. Several interviews were conducted in specific departments such as Planning, Building, Code Enforcement, Police and Fire to first identify possible ideas of new fees or areas where fees could be raised to better reflect costs. This emphasis was chosen because raising existing fees is both quicker and easier to implement. If a fee is already in place for a service and a process to collect it has been established, raising the fee has fewer implementation obstacles than the establishment of a new fee. However, additional legal analysis will be required in the implementation phase of all of these fees. Having said that, there are instances where a new fee may be warranted in order to address the City's costs for providing services and the process of establishing the new fees should begin as soon as possible.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

Some existing fees mentioned here have been in discussion with related internal and external stakeholders long before the current work began and may be included in the 2008-2009 Proposed Budget. Other fees have been discussed at various times and should now be fully reconsidered in light of the Structural Budget Deficit. Existing fees which should be reconsidered for increasing to full cost recovery for Category I and increasing for Category II fees based on increases in prices to provide services. In some instances, services have modified or increased over time but fees have not been established to cover those costs. Pursuant to long established City Council policy, the City should regularly examine new opportunities to attain full or partial cost recovery for services over time. The chart below outlines a series existing fees and new fees ideas developed. Although not a comprehensive list, the fees should be considered.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

Fee Description	New or Existing Fee	Requires Further Legal Analysis	Requires Further Implementation Analysis	Estimated Fiscal Impact Estimate
Advance Planning Fee ¹	Existing	No	No	\$400,000
PRNS Facilities Rentals ¹	Existing	No	No	\$44,000
Parking/Meter Fees	Existing	No	No	\$500,000
Fingerprinting (sex offenders, arson and narcotics parolees) ¹	Existing	Yes	Yes	TBD
Visa/Immigration Clearance Letters	Existing	Yes	Yes	TBD
Non-Public Records Act Copy Charges ¹	Existing	Yes	No	TBD
Animal Care and Services Miscellaneous Permits ¹	Existing	No	No	\$2,500
Taxi Cab Public Safety Permits ¹	Existing	No	No	\$90,000
Record Sealing	New	Yes	Yes	TBD
Entertainment Zone Policing Plan (to fully enact)	New	Yes	No	\$400,000-\$600,000
Fire Inspections for Covered Malls	Existing	No	No	TBD
Fire Protection System Permit and Inspection	New	Yes	Yes	TBD
Business Tax Administrative Fee ²	New	No	No	\$1,400,000
Litter Fee	New	Yes	Yes	\$200,000
Police Department Subpoena Compliance	New	Yes	Yes	TBD
Non Public Records Act Copy Charges for archived records	New	Yes	No	TBD

¹Fees are Category I Full Cost Recovery²New Fee in 2008-2009 Proposed Fee and Charges Report

In conjunction with completion of the Three-Year Structural Budget Deficit Elimination Plan in November of 2008 budget staff will be developing recommendations to adjust the fees referenced above and returning to Council with an appropriate recommendation when any further analysis required is completed during 2008-2009. In view of the need to generate additional revenues staff may not wait until development of the annual update of fees in June 2009.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

In some instances, services have modified or increased over time but fees have not been established to cover those costs. Pursuant to long established City Council policy, the City should regularly examine new opportunities to attain full or partial cost recovery for services over time.

Finally, there are instances where raising fees can manage demand for City services. In these instances, services could be considered voluntary or not necessary to live and work in the City. For example, Planning, Building and Code Enforcement Department instituted a fee to obtain preliminary project review services. Previously, the staff provided near unlimited free service members of the real estate and development profession to enhance their services. On the other hand, the cost of providing the service and level of demand for it were resulting in rising costs for the balance of the fee paying customers of the Department. After initiating the fee, requests were significantly reduced. When examining fee for services, especially those below full cost recovery the City should consider that even modest increases can reduce demand for non-essential services and can save the City more by reducing demand rather than creating revenue. City management will examine this issue in conjunction with development of the 2009-2010 fee recommendations.

The potential to increase General Fund revenues by instituting all the fees identified above would be an additional \$3 to \$4M annually. In addition fiscal impacts for several fees are not yet estimated, nor has the implementation of a full cost allocation analysis been factored into the results. It will take time to fully implement all fee improvements but within a Three-Year timeframe substantial improvements can be made. The Three-Year Structural Budget Deficit Elimination Plan to be presented in November, 2008 will further quantify the opportunities to generate additional revenues and reduce service demand costs.

Changes in fees are enacted by the City Council. For those fees that still require more internal discussion and external stakeholder outreach, the process should begin now to ensure analysis and support is completed for the 2009-2010 budget cycle.

Strategy: Implement Citywide Lighting and Landscaping District or Proposition 218 "Property-Related" Fees

The use of Lighting and Landscaping Districts (LLD) as a funding mechanism is common among many of the peer jurisdictions. A LLD is authorized by the State Landscaping and Lighting District Act of 1972. An LLD allows local governmental agencies to form maintenance districts to finance, install, construct, and maintain landscaping, lighting and transportation infrastructure, and park and recreation facilities. Currently within the City of San Jose many of the above types of services are funded via the General Fund, although the City also has numerous LLDs associated with individual development.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

A menu of possible services that could be funded through a Lighting and Landscaping District (LLD) pursuant to Proposition 218 has been identified. The services under consideration to be funded through an LLD include but are not limited to replacing street lights with more efficient fixtures as well as pruning existing street trees, sidewalk repair and curb and gutter repair, which are currently the full responsibility of property owners because the City has eliminated funding used to assist property owners on maintaining these assets. Additionally, the district could also cover street landscaping maintenance, which has been significantly reduced with more reductions anticipated, and achieve half the goal of the Citywide Green Vision Plan by planting 50,000 street trees in park strips where trees are missing.

With regard to other services, such as traffic signal and pavement maintenance, the City is pursuing regional, state and federal funding, and other revenue sources to address the backlog of deferred maintenance in areas, but these services also might be addressed via the LLD strategy in order to relieve costs on the General Fund.

The key distinction between an assessment and other types of revenue measures, such as fees and taxes, is that an assessment is levied as a charge for the special benefit that a property will derive from the improvement or service provided by the assessment. The classification of a charge as an assessment, rather than as a tax or a fee, is important because Propositions 13 and 218 provide for drastically different substantive procedural and voter approval requirements for assessments than for taxes and fees.

The Lighting and Landscaping District is being considered for implementation on a Citywide basis. This is primarily because it is important to provide some consistency and equity in the delivery of basic City services. The Engineer's Report that forms the basis of the assessment must evaluate the benefit to each parcel of property in the entire City in order to justify the level of assessment on each parcel or type of parcel. A Citywide Lighting and Landscaping District could raise approximately \$20-\$30M which would, overtime, reduce the unmet/deferred infrastructure and maintenance portion of the structural budget deficit.

Jurisdictions have successfully voted to continue assessment districts following passage of Proposition 218, and, in the case of San Ramon, Pittsburg and Danville, the property owners have voted to increase assessments. Oakland was unsuccessful in getting an increase approved in 2006, but is currently in the process of going back to the property owners to increase assessments. Sacramento has built in a cost of living adjustment each year to cover increasing costs.

Implementation of a new Lighting and Landscaping District requires Council approval and a vote of property owners within the district following the provisions outlined in Proposition 218. Fees for an assessment district may not be imposed unless a local government conducts a majority protest proceeding 45 days after a mailed notice to all persons subject to the assessment. If no majority protest occurs, then the agency must submit the measure to a mailed ballot to

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

property owners. Only returned ballots are counted. Each ballot is weighted based on the amount of the proposed assessment on the parcel.

The City would need some one-time additional funding to fully develop and implement an LLD including the feasibility study and parcel analysis, preliminary service and assessment analysis, and public survey work, the engineer's report, and the actual mail ballot process. In 2008-09, resources would be required to conduct the preliminary feasibility analysis.

It should be noted that the Stakeholder Group expressed interest in broadening this idea to include smaller improvement districts that could be tailored to the interests and needs of a neighborhood. Staff will develop a policy discussion on this concept for Council consideration when we return in November.

Strategy: Restructure Business Tax to Modernize and Reflect Current Business Profile

The City's business tax was adopted in 1984 and the rate has remained unchanged since that time. Consequently the share of General Fund revenues derived from this revenue has declined from 1.9% of the General Fund total in 1984 to 1.2%. Annually, the City collects approximately \$13-\$15M in revenues from the Business Tax.

According to California State Law, general law and charter cities are allowed to levy a tax on business activity. Throughout the State, the nomenclature for such taxes varies, but is most commonly referred to as business taxes, business license fees, or business permits. A business tax may be fixed amounts based on a per unit basis or may be based on the number of employees, gross receipts, net business income, and/or the number of rental units (for landlords). In regard to the overall business tax structure for municipalities, there is no consistent structure among the San José large city peers and the City's neighboring municipalities. Six of the ten largest cities in California (by population) have complex business tax structures with a variety of discrete business categories. The cities of San José, San Diego, Sacramento and San Francisco are the exceptions with few categories. Like San José, San Diego and Sacramento separate businesses into four or fewer categories. Of the nine San José peer cities, only the City of Oakland has a business tax structure that includes a payroll tax for certain types of businesses. The City/County of San Francisco also has a payroll tax.

San Jose is below other large peer cities (San Diego, Los Angeles, San Francisco, and Oakland) in business tax rates on a per capita comparison. In considering rates, San Jose not only looks at other large peer cities, but also considers the rates in other Silicon Valley cities. The rate in San Jose is higher than surrounding cities.

Two options were analyzed for this strategy: modernize the business tax rates by indexing the rates to the current Consumer Price Index (CPI) or restructuring the business tax formula, including whether to increase the cardroom tax.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

Option A: Index Rates to Current CPI and Raise Minimums

The City of San José's business tax rates are at the same level today as they were in 1984 when Ordinance 25182 established the current business tax structure. In November 1996, the rates were increased to reflect an annual inflation factor as a result of recommendations from the "New Realities Task Force". Retention of the new rates was contingent on voter approval. The voters did not approve the continuation of the increased rates in November 1998 and the rates were returned to their 1984 level.

Because the business tax rate has not changed since 1984, the tax's contribution to the General Fund is diminished by inflation. If indexed by the CPI from 1984 to 2007, the base rate for the tax would increase from \$150 to \$301 and the rate for each employee above eight would increase from \$18 to \$36.

Revising the tax structure from 1984 to 2008 dollars to fully account for inflation would approximately double current revenues (an addition of approximately \$13-15M per year). To index the business tax structure from 1984 to 2008 dollars, the City will be required to obtain majority voter approval for the changes. A majority vote of the Council would also be required to place the measure on the ballot.

Option B: Restructure Business Tax

San Jose has the opportunity to evaluate and modernize the business tax structure. Alternative approaches used by other jurisdictions include a tax based on income, employment or by industry type.

The income approach offers two options: net business income and gross receipts. The City of Portland, Oregon uses the net business income approach and the City of Los Angeles uses the gross receipts approach, as does the City of Pleasanton in the Bay Area. Further analysis is required to determine the potential revenue that would be generated from either a net business income or gross receipts approach. In considering such an approach, the required staff and reporting structure to be able to collect revenue information from the over 64,000 businesses now paying business taxes will also need to be analyzed.

The employee approach establishes a rate based on either a base rate for a minimum number of employees and a per employee rate thereafter (the approach currently used by the City of San Jose) or by employee groups (i.e., 1-4, 5-10, 10-20 employees, etc.). The State of Nevada charges an employee tax rate of \$25 per employee. Santa Clara charges by employee groups. Santa Cruz and Milpitas charge a minimum rate and a per employee rate thereafter. Indexing the current minimum and rate per employee to the current CPI would generate an additional \$13-\$15M for the City of San Jose. Currently, businesses self-report number of employee information to the City.

ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

The industry approach is a rate based on industry type (i.e., retail, commercial, industrial). Few cities in California use this method for calculating business tax. The estimate for additional revenues to the City's General Fund using this approach is \$6-\$8M.

The San José business tax structure includes a 13% cardroom tax. An additional \$1.8M would be generated if the cardroom tax were to be increased from 13% to 15%.

Restructuring the business tax would require extensive outreach with business groups to determine the most equitable structure for the tax and the impacts on businesses. This outreach would likely take 12-24 months and a measure could not be placed on the ballot until June or November 2010. A majority vote of the Council is required to place the measure on the ballot and a majority electoral vote is required to implement a restructured tax method.

Strategy: Increase Sales Tax to Provide Increased General Fund Revenues

The use of sales tax to fund specific or general services is common in California. Often such taxes are used to fund some enhancement in service level or to avoid specific cuts. Considerable latitude is allowed for a city to design a tax to fund both ongoing and new services. If the increase in sales tax is to fund specific purposes, a 2/3 vote is required. If the increase in sales tax is to fund the agency's general purposes, then the measure requires a simple majority.

San José currently receives one cent of the total 8.25 cent sales tax that is applied to all sales in in Santa Clara County. This one cent local agency allocation based on 2006-2007 actual receipts, results in the City receiving approximately \$125M in General Fund revenues. Raising the City's sales tax rate by .25 cent would raise approximately \$21M in annual revenues. While the basic 8.25% sales tax rate in Santa Clara County is relatively high by California standards, it is actually low relative to Bay Area peers. San Francisco's sales tax rate is 8.5% and in Oakland and Fremont the sales tax rate is 8.75%. This comparison suggests that the potential may exist to propose a .25 cent sales tax in San José without a major anti-competitive impact. If a sales tax measure were to go forward for San Jose, it would result in a rate different from that of other cities in Santa Clara County. However, twenty-two counties in California have cities with different sales tax rates, including Santa Cruz, Monterey, Fresno, Marin and Yolo Counties.

Since 2004, thirty-four general purpose sales tax increase measures have passed and twenty-four have failed. Inglewood, San Louis Obispo and Santa Cruz approved a .50 cent sales tax increase. San Bernardino and Watsonville approved a .25 cent sales tax increase and Hollister and Seaside approve a 1.00 cent sales tax increase (Hollister's increase is for five years).

In November 2004, the City of Santa Rosa successfully passed a .25 cent sales tax for police, fire and youth services. It is generating an estimated \$7 million per year for this City of approximately 170,000 people. The special tax was passed by slightly more than a 70% majority. The funding was allocated to fund police and fire positions that would otherwise have been eliminated, to generate funding for new facilities and equipment and to fund gang prevention and

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ANALYSIS OF TOP PRIORITY STRATEGIES (CONT'D.)

youth programs. In November 2007, two cities (Selma and Ceres) proposed .50 cent sales tax levies to fund safety services. Both passed with more than 75% approval. Seven cities placed a voter initiative proposing a general sales tax (majority vote required). Three of the seven measures passed.

A major complication with this strategy is that a sales tax increase may be considered in November 2008 as a revenue source to fund other public services in Santa Clara County ranging from health care to transportation. The City of San José may confront regional opposition to placing a local measure on the ballot in the face of so many other competing measures.

Implementation of this strategy would require a 2/3 vote of the City Council to place on the November 2008 ballot. If placed on the ballot as a general purpose tax, a majority electoral vote would be required.

COORDINATION

This MBA has been coordinated with the City Attorney's Office and with the Redevelopment Agency Executive Director.

/s/
Debra Figone
City Manager

STAKEHOLDER GROUP MEETING – SYNOPSIS

MEETING DATE: 4/21/2008

ATTENDEES: PETE CONSTANT, CHAIR

MEMBERS: LORIE BIRD, ELIZABETH BRIERLY, CARL COOKSON, YOLANDA CRUZ, PAT DANDO, PATRICIA GARDNER, ERNIE GIACHETTI, HOOSHANG HOMARA, JOSHUA HOWARD, CHARLES JONES, MICHELLE LEW, BOBBIE LOPEZ, STEVE MOORE, DAVE PERSSELIN, ED RAST, JEFF RUSTER, JAN SCHNEIDER, RANDY SEKANY,

BUU THAI, KEN WILLEY, SUZANNE WOLF

ABSENT: BOB BROWNSTEIN

RESIGNED: LISA RIGGS, KERI PROCUNIER McLAIN

STAFF: DEBRA FIGONE, CITY MANAGER, HARRY MAVROGENES, EXECUTIVE DIRECTOR REVEVELOPMENT AGENCY, JANE LIGHT, CITY MANAGER'S LIAISON, SHAWN SPANO, FACILITATOR.

Welcome/Introductions/Process Overview

- Councilmember Constant called the meeting to order at 6:05 p.m. by welcoming everyone.
- The City is in its seventh year of budget deficits with many more years of projected deficits ahead.
- The Stakeholder Group will look at the urgent strategies that have already been identified, but can also propose other strategies that have not yet been identified.
- City Manager Debra Figone stated her role is to listen carefully, ask questions, and interject when helpful. The Structural Budget Deficit is an important task to address because the deficits are preventing the City from providing the level of service the City wants to provide. City staff is flexible and adaptable to ensure this process fits the City and Stakeholder Group needs. Staff presentations will give context but are not meant to limit or be a to barrier thoughts.
- City Manager Figone clarified that the Council must take action by August 5 Council Meeting to put items on the November 2008 ballot.
- Councilmember Constant stated the Stakeholder Group will meet in July despite legislative break to discuss time-sensitive issues.
- Stakeholder Group members introduced themselves.
- Shawn Spano will facilitate meetings to help the group cover all of the information needed and guide the conversations. He is a Professor in the Communications Department at San Jose State University and a consultant.

“SETTING THE MEETING CONTEXT” Presentation

(<http://www.san Joseca.gov/StakeholderGroup08.asp>) (Slides 2-5).. April 21 Presentation: Shawn Spano

- Overview of the six-month process and purpose of 4/21/08 meeting. Step 1 of the process will begin today. Discussion of advantages and concerns of the Urgent Strategies.
- Steps 2 and 3 will follow in June and will cover advantages and concerns of the remaining identified strategies, as well as other strategies that the group may identify.
- The group represents diverse interests, perspectives, and expertise. The goal is to bring this diversity together to come up with ideas that represent the knowledge of all the stakeholders at the table.
- Stakeholder Group input will be included in the City Manager’s 3 Year General Fund Structural Deficit Elimination Plan report that will go to the Council in November.
- Presentations on 5 of the 10 urgent strategies will be discussed at this meeting. The focus is to provide a context and framework to understand these strategies
- At the end of each presentation the Stakeholder Group will ask questions and then list the “Advantages and Concerns”.
- The materials included in the Stakeholder Group binders and cited with weblinks on the meeting agenda provide extensive information.
- Meeting schedule was reviewed. All meetings are in the Committee Rooms at City Hall (Wing 118-120) except on April 28 and September 22. On these dates the meeting will take place at the King Library, Room 229 (2nd floor). Meeting attendees can park at City Hall garage or Fourth Street garage (4th Street and San Fernando) and receive parking validation.
- Absences will be excused if you email in advance Councilmember Constant (pete.constant@san Joseca.gov) or Jane Light (jane.light@san Joseca.gov).

“PREPARING TO DISCUSS STRATEGIES” Presentation: Shawn Spano

(<http://www.san Joseca.gov/StakeholderGroup08.asp>). April 21 Presentation (Slides 4-5).

- Staff will talk about budget strategies; provide objective analysis to provide information to the group.
- The group will drive the conversation. Staff is prepared to go deeper, if you want staff to clarify information. Staff is also prepared to give the group evaluation of the strategies. It will depend on the level of discussion the group wants.

- Councilmember Constant asked the group to focus on the concept of the strategy rather than on implementation details.
- Group is here to discuss Questions/Concerns/Advantages of the proposed strategy.

“INTRODUCTION TO THE GENERAL FUND DEFICIT ELIMINATION PROJECT “

Presentation: Andy Belknap, Management Partners

(<http://www.sanjoseca.gov/StakeholderGroup08.asp>). April 21 Presentation (Slides 6-18).

Belknap reviewed the components of the deficit, revenue and expenditure trends, the categories into which strategies fall, and the list of those strategies that fall into the “Timing Urgency” and “Immediate Opportunity to Implement” All the strategies are consistent with Council goal of eliminating the budget deficit. That ruled out a lot of the economic development strategies, because those take time to produce revenue results.

Urgent Strategy 1A “UTILIZE FINANCIAL STRATEGIES THAT HAVE POSITIVE NET PRESENT VALUE.” (<http://www.sanjoseca.gov/StakeholderGroup08.asp>). April 21

Presentation (Slides 19-30). Scott P. Johnson, Finance Director

STRATEGY		1A: Utilize Financial Strategies that have positive Net Present Value (NPV) : Annual Prepayment of city’s Pension Obligation		
	ADVANTAGES			CONCERNS
1.	Less administration?		1.	Less administration?
2.	Pension funds invested for – greater ROI than City’s Timing & discount		2.	“True Up” reconciliation at year end – overpayment details
3.	Retirement funds have good record of making/exceeding planned returns & stable returns		3.	Cash flow
4.	Could be done one year at a time		4.	Financial Risk – All funds for year invested at one time (no dollar cost averaging)
5.	Rate of Return for City is now about 4.6%; retirement funds get substantially higher rate			

Urgent Strategy 1B “UTILIZE FINANCIAL STRATEGIES THAT HAVE POSITIVE NET PRESENT VALUE”. (Slides 19-30) (<http://www.sanjoseca.gov/StakeholderGroup08.asp>). April 21 Presentation (Slides 30-36). Scott P. Johnson, Finance Director

STRATEGY		1B: Utilize Financial Strategies that have positive Net Present Value (NPV) : City to Issue Pension Obligation Bonds		
	ADVANTAGES			CONCERNS
1.	Create jobs for San Jose		1.	Outsource versus in-house; additional staffing resources required
2.	Bond rate fluctuations could be a benefit if they go lower		2.	If interest rate increases, lose some savings –at risk for interest rates spike
3.	City can time bond issuance to be favorable		3.	Cost to issue, administer debt service, etc. (analyze gross & net costs to know all costs)
			4.	Would it have impact on City’s bonding capacity?
			5.	Using return as credit that reduces City contribution/”smoothing” policy over 5 years

Smoothing Policy: Any gains or losses over or above on any assumed rate of return are captured in the actuarial and smoothed over a 5 year time period. We assume City's current policy of smoothing gains. For example, if we assumed 8% and got 13%, we would only credit 1% for 5 year.

Stakeholder Suggestion: As a new strategy, can we look at Smoothing? Concern is how the smoothing works & can it be done differently to reduce deficit?

Stakeholder Suggestion: What if we reduce our "funding" target on the Police Plan, since we are so close to full funding, and then take that money to fund GASB requirements?

Urgent Strategy 2 "FORMALIZE AND IMPLEMENT A RIGOROUS

ASSETMANAGEMENT PROGRAM" Presentation: Katy Allen, Public Works Director

(<http://www.sanjoseca.gov/StakeholderGroup08.asp>) April 21 (Slides 31-37).

STRATEGY		2: Formalize and Implement a Rigorous Asset Management Program		
	ADVANTAGES			CONCERNS
1.	Could break asset management into pieces and implement over time – get some fast-tracked for "big bucks" results		1.	Facility rent/use by nonprofits: <ul style="list-style-type: none"> - Facility occupancy, full/partial? - Community center reuse - Long-term plan for development
2.	Mgmt Partners report: \$15M (up to) for sale of property +/- \$3M per year for add'l rent/lease income		2.	Address key issues of use/business via policies
3.	Policy makes it possible to manage assets, overlay with inventory		3.	Look at 'Sunshine' definition of tax subsidies
4.	Potential of longer leases, more stability for nonprofits		4.	Lease facilities under-utilized – look at more shared bldgs, include in inventory the market rate
5.	Look at private enterprise help – expertise here		5.	Outsource versus in-house costs for program development and management
6.	Maximize use of facilities – partnerships, etc. – combined uses		6.	
7.	Consider looking at zoning etc, to expedite and maximize		6.	Re-investing savings to enhance remaining properties – should be included in analysis
8.	Prioritize largest most valuable assets		7.	Consider limitations of assets (size of convention center, specialized use facilities) include in analysis
9.	Policy could look at businesses City is in – should City be in the business or not?		8.	Businesses involved – do we need to be in that business
10.	Dovetail Asset Management Policy with Facilities re-use policy		9.	Timing of strategy too long – should be 2-3 month timeline

Urgent Strategy 3 “IMPLEMENT AN EMPLOYEE SUGGESTION AND PROCESS STREAMLINING PROGRAM” Presentation: Mark Danaj, Human Resources Director (<http://www.sanjoseca.gov/StakeholderGroup08.asp>) (Slides 38-44). This strategy was referenced in the Management Partners Report under Service Delivery Model Change #7pp 94-98.

STRATEGY		3: Implement an Employee Suggestion and Process Streamlining Program		
	ADVANTAGES			CONCERNS
1.	Capture ability and knowledge of employees		1.	Timing between suggestion and evaluation feedback – timely response required
2.	Energizing to employees		2.	Program laying dormant for last 5 years – constant marketing, evaluation needed
3.	Gives employees power over things that frustrate them		3.	Employee engagement – in spite of morale – leadership from administration to encourage engagement
4.	Opportunity to interact with other depts and with City Senior Staff		4.	Need venue outside department for ideas to be considered
			5.	Allow employee to be part of implementation – morale improvement

Urgent Strategy 4 “ENSURE CURRENT FEES FULLY COVER ALL COSTS” Presentation: Joe Horwedel, Director of Planning, Building and Code Enforcement (<http://www.sanjoseca.gov/StakeholderGroup08.asp>). (Slides 45-51) Management Partners Report, pp66-68.

STRATEGY		4: Ensure current fees fully cover all costs		
	ADVANTAGES			CONCERNS
			1.	Blurred line between fees & taxes
			2.	Don't charge fees for City core services
			3.	Don't create fees that lead to administration fee to get to cost recovery
			4.	Fees getting in the way of Job formation, retention, growth
			5.	Making it difficult for growth in retail sales tax, jobs
			6.	Raising fees could deter business
			7.	Bus Tax Admin Fee should be considered with restructure of Business Tax
			8.	Surpluses of fees collected – bring in line with expenses
			9.	Business inquiry that don't come back because of costs
			10.	Balance – unintended consequence of losing businesses
			11.	Attacking small businesses

Advantages/concerns/questions can be emailed to pete.constant@sanjoseca.gov in the subject line write Stakeholder Group. He will forward questions to the administration.

Public Comment: Councilmember Pierluigi Oliverio addressed the group, thanking Stakeholder Group members for their service. Encouraged members ask hard questions to find a nonpolitical solution to this budget deficit.

Closing: Next meeting on April 28 will be held at the Dr. Martin Luther King Jr. Library. The discussion of Urgent Strategies will be continued. Members were thanked for their time and service. Meeting was adjourned at 9:05 p.m.

STAKEHOLDER GROUP MEETING – SYNOPSIS

MEETING DATE: **4/28/2008**

ATTENDEES: COUNCILMEMBER PETE CONSTANT, CHAIR

MEMBERS: LORIE BIRD, ELIZABETH BRIERLY, BOB BROWNSTEIN, CARL COOKSON, PAT DANDO, PATRICIA GARDNER, ERNIE GIACHETTI, HOOSHANG HOMARA, JOSHUA HOWARD, CHARLES JONES, MICHELLE LEW, BOBBY LOPEZ, STEVE MOORE, DAVE PERSSSELIN, ED RAST, JEFF RUSTER, JAN SCHNEIDER, RANDY SEKANY,

BUU THAI, KEN WILLEY, SUZANNE WOLF

ABSENT: YOLANDA CRUZ

STAFF: DEBRA FIGONE, CITY MANAGER, HARRY MAVROGENES, EXECUTIVE DIRECTOR REVEVELOPMENT AGENCY, JANE LIGHT, CITY MANAGER'S LIAISON, SHAWN SPANO, FACILITATOR.

Welcome/Introductions/Process Overview

- Councilmember Constant called the meeting to order at 6:09 p.m. by welcoming everyone and asking Stakeholder Group members to introduce themselves.
- Shawn Spano will continue to facilitate the discussion. Each strategy now has time allotments assigned to ensure the group gets through the agenda.

Meeting Agenda Review/Future Meetings/Process

(<http://www.sanjoseca.gov/StakeholderGroup08.asp>) (Slides 2-4). April 28 Presentation: Shawn Spano.

- Urgent Strategies #4, #5, #7, #9 will be discussed tonight.
- Urgent Strategies #6, #8, #10 will be discussed on May 5.
- Focus on advantages and concerns of strategies. Questions and clarifications are welcomed.

Urgent Strategy 4 “Ensure Current Fees Fully Cover All Costs”

Presentation:

Larry Lisenbee, Budget Director Emeritus (<http://www.sanjoseca.gov/StakeholderGroup08.asp>).

(Slides 5-15)

Management Partners Report Revenue Strategy #3 pp 66-68.

Presentation and discussion continued from April 21 meeting.

STRATEGY		4: Ensure current fees fully cover all costs			
	ADVANTAGES				CONCERNS
1.	Fees give City capacity to accomplish a number of things		1.		Fee differences with surrounding cities/competitiveness
2.	Provide the opportunity to raise revenue for specific programs/items that require an extraordinary level of service than is being demanded elsewhere		2.		Discussing fees in isolation of understanding what it costs to provide service or what it costs to live in San Jose compared to other jurisdictions
3.	Fees to provide services that the City has no regulatory obligation to provide (e.g. golf courses)		3.		What is benchmark for when fees were set? In which cases have the fees not been increased in a long time?
4.	Mechanism that provides flexibility and discretion to make minor regulatory changes without going to the voters		4.		Competitiveness study should be done before making recommendation on fee increases
5.	Fees offer opportunity to share the benefit of monopoly businesses –Sole source service providers that are making money (e.g., ambulance provider)		5.		Is the City tracking/charging all the fees on the books? Examples – repeated false alarms; party response fee (Police Dept.)
6.	Increased fees could result in higher level of service		6.		Market distortions could discourage business
			7.		Do not subsidize fees in a way that encourages poor decision-making by businesses

Stakeholder Question: Can we get a list of all fees that have not been increased in five years?

Stakeholder Question: Are there other things like fee/loan forgiveness or other incentives to invest money, generate jobs, and/or bring revenue? Want to see list of out of the box thinking for forgiveness.

Stakeholder Question: What can we do to help retail/car dealerships be successful?

Stakeholder Question: Which fees that are on the books are not actually collected?

Urgent Strategy 5 “Implement City-Wide Landscape and Lighting District or Other Proposition 218 Property-Related Fees”.

Presentation: Jim Helmer, Department of Transportation Director

(<http://www.sanjoseca.gov/StakeholderGroup08.asp>) April 28 (Slides 16-22).

Management Partners Report Revenue Strategy #6 pp 74-76.

STRATEGY		Implement City-Wide Landscape And Lighting District Or Other Proposition 218 “Property-Related” Fees		
	ADVANTAGES			CONCERNS
1.	Some neighborhoods would welcome opportunities to get increased quality in neighborhood and business services – a trial or model program to test results and interest in participating		1.	How/who determines what is needed in landscaping, sidewalks, etc.
2.	Might be an opportunity for a new model – do a pilot.		2.	Are all parcels (residential and commercial) assessed?
3.	Improve the ambiance/quality of the entire City.		3.	Why not include parks?
4.	Shared risk of fixing sidewalks – opportunity to buy into “sidewalk repair insurance”. Make it voluntary- those who don’t pay have to pay out of their own pocket for the repair.		4.	How would this work in redevelopment neighborhoods? How is it decided where you plant trees, put the lighting?
5.	Address specific needs of neighborhoods- encourage neighborhood meetings to help set priorities, decision making.		5.	Need to be able to address specific needs of a neighborhood – different in different neighborhoods in the city.
6.	PBID sharing advantages already.		6.	Will be perceived as a tax because it is on the property tax bill.
7.	Quicker turn-around time for improvements.		7.	How would this impact the schools and would the schools be participating in the costs?
8.	Elicit more pride in neighborhoods.		8.	Define how big a neighborhood is.
			9.	Can this be implemented as a neighborhood pilot? Citywide assessment might fail. Show results at a neighborhood level first.
			10.	Could the city just enforce property owner responsibility for sidewalk and street tree maintenance/repairs?

Stakeholder Question: Will the Lighting and Landscape Assessment be tax deductible? (Since you pay with it with your property tax bill).

Stakeholder Question: How many “trip and fall” incidents and/or claims in the City?

Urgent Strategy 7 “Shift Revenues from Construction and Conveyance Taxes from Capital Projects to Operations and/or Raise Conveyance Tax”

(<http://www.sanjoseca.gov/StakeholderGroup08.asp>) April 28 (Slides 31-37). Presentation: Ed Shikada, Deputy City Manager.

Management Partners Report Expenditure Controls and Shift Strategy #3 pp. 104-108

- The wording of this Urgent Strategy has been changed from the language in the Management Partners report to reflect that Construction & Conveyance are two different taxes.
- The graph on Slide 25 is also different from the graph on page 105 of the Management Partners report.

STRATEGY		7: Shift Revenues from Construction and Conveyance Taxes from Capital Projects to Operations and/or Raise Conveyance Tax		
	ADVANTAGES			CONCERNS
1.	Options A & B give the City more flexibility on whether to spend on maintenance or capital.		1.	Concern over competitiveness with surrounding cities.
2.	Option B - Voters would agree with shifting to maintenance v. increasing.		2.	Extra fees would affect property buyers.
3.	Options A & B allow more flexibility for park maintenance.		3.	Option B – Does it make sense to go to voters if we are not getting new revenues?
4.	Option B – easiest to explain to the community. Might agree to a one time increase at time of sale.		4.	Might affect sales and construction.
5.	If going for vote – need to ask for a raise in the Conveyance tax.		5.	Start to change fees structure, really don’t know impact.
6.	Doesn’t hit the property owner every year, only when you sell – not as onerous.		6.	Over last 20 years, have had built in increases because of increasing property values.
7.	Option A – brings new revenue.		6.	Problem justifying Options B & C.
8.	Tax deductible?		7.	Option C – Council would not allow it to go on the ballot.
9.	If increase is a general tax, only requires a majority vote.		8.	Parks allocation only – really need maintenance for what we built.
10.	Could categorize structure of fee by : -level of appreciation/depreciation -length of ownership		9.	Are revenue estimates for current and future years too high? (given market outlook)
			10.	Increase in property value brings revenue in C&C revenue anyway.
			11.	No net increase to revenue unless we raise the fee.

Stakeholder Question: Can we incorporate transportation maintenance needs into the services covered by the Construction & Conveyance Tax?

Public Speakers:

Parks and Recreation Commissioner spoke in support of Option A, and submitted a letter to the Chair stating their support. The Commission believes that Option A supports multiple departments, does not affect all people at all times (only at time of sale) and is tax deductible. Library Commissioner spoke in support of keeping Library portion of the C&C separate. This money supports library materials.

Urgent Strategy 9 “Increase Sales Tax to Provide Increased General Fund Revenues”

Presentation: Scott Johnson, Finance Director

(<http://www.sanjoseca.gov/StakeholderGroup08.asp>) (Slides 38-44). Management Partners Report Revenue Strategy #7pp 76-78.

STRATEGY		9: Increase Sales Tax to Provide Increased General Fund Revenues		
	ADVANTAGES			CONCERNS
1.	This is a general tax, so it requires only a majority vote (50% +1)		1.	Possible loss of sales due to increased tax.
2.	Strategy ensures that the percentage of the sales tax raised locally stays local.		2.	Development costs combined with higher sales tax will impact small business.
3.	Tax is based on purchases bought or used in San Jose.		3.	Sales tax is regressive. It will hit those with limited income.
			4.	Will drive sales to Cities surrounding San Jose.
			5.	Need to balance tax increases with other strategies.
			6.	Don't load up the ballot with too many revenue measures.
			7.	Increased gas costs generate more sales tax from that source.
			8.	State may look to this source as well – everyone going after same pot of money.
			9.	Competition with the internet.
			10.	New revenues do not account for potential loss of sales.
			11.	Recent County/VTA sales tax was defeated.
			12.	Should look at streamlining permits, development process rather than raising sales tax.
			13.	County and VTA looking at an additional sales tax (may have to work with them on a strategy).

			14.	Need to bring in more sales volume – problem attracting businesses.
			15.	Many people who live in San Jose are working in other places, will buy where they work rather than where they live.
			16.	Taxpayers feel very strongly – no new taxes.
			17.	City has turned away big box.

Correction to Slide 35 “Potential Fiscal Impact”: A ¼ percent “San Jose District Sales Tax” will increase revenue by \$21 Million dollars. The information presented at the Stakeholder Meeting stated that \$14.5 Million dollars of revenue would be generated by the tax increase.

Stakeholder Question: Eliminating binding interest arbitration also requires voter approval (since it is a Charter Amendment), why is this strategy not on the urgent list?

Stakeholder Suggestion: Check revenue calculations- is it a 1/8 or 1/4 percentage increase?

Stakeholder Question: Is there data on the drop in sales tax revenues connected to the sales tax experienced by other cities?

Stakeholder Question: Can we have a break down of the sales tax by source. For example, sales tax from cars, retail, etc. Councilmember Constant stated the City has that information, and has it by Council District as well.

Stakeholder Question: Why are most of the urgent strategies taxes? Councilmember Constant and Bob Brownstein explained that decisions must be made by the Council soon about any November 2008 ballot measures. The next opportunity for ballot measures will not be until 2010.

Closing: Next meeting will take place on May 5 at City Hall, Wing Rooms 118-120. The discussion of Urgent Strategies will be continued. Members were thanked for their time and service.

Advantages/concerns/questions can be emailed to pete.constant@sanjoseca.gov, please type “Stakeholder Group” in the subject line. Councilmember Constant will forward questions to the administration.

Meeting was adjourned at 8:50 p.m.

STAKEHOLDER GROUP MEETING – SYNOPSIS

MEETING DATE: **5/5/2008**

ATTENDEES: COUNCILMEMBER PETE CONSTANT, CHAIR

MEMBERS: LORIE BIRD, ELIZABETH BRIERLY, BOB BROWNSTEIN, CARL COOKSON, YOLANDA CRUZ, PAT DANDO, ERNIE GIACHETTI, HOOSHANG HOMARA, JOSHUA HOWARD, CHARLES JONES, MICHELLE LEW, BOBBY LOPEZ, STEVE MOORE, DAVE PERSELIN, ED RAST, JAN SCHNEIDER, RANDY SEKANY, BUU THAI, KEN WILLEY, SUZANNE WOLF

ABSENT: PATRICIA GARDNER, JEFF RUSTER,

STAFF: DEBRA FIGONE, CITY MANAGER, HARRY MAVROGENES, EXECUTIVE DIRECTOR REVEVELOPMENT AGENCY, JANE LIGHT, CITY MANAGER'S LIAISON, SHAWN SPANO, FACILITATOR.

Welcome/Introductions/Process Overview

- Councilmember Constant called the meeting to order at 6:09 p.m. by welcoming everyone and asking Stakeholder Group members to introduce themselves.
- Shawn Spano will continue to facilitate the discussion. Update on information requests was included in the slide presentation and a review of the strategies to be discussed was provided. (<http://www.sanjoseca.gov/StakeholderGroup08.asp>) May 5, 2008 (Slides 2-7).

Meeting Agenda Review/Future Meetings/Process

- Urgent Strategies #6, #8, #10 will be discussed tonight.
- Focus on advantages and concerns of strategies. Questions and clarifications are welcomed.
- Stakeholder Group members were encouraged to attend the City Council Study Session on May 16, 9:00 am in the Council Chambers.
- Discussion about handouts included question regarding recent Business Journal article about card clubs and growth potential which could positively impact revenues.
- Concern was raised about not recording meetings electronically. There was concern about tonight's voting exercise, so the methodology was changed to address concerns. Discussion about the State budget impacts on legislative strategies which may trickle down to City budget impacts was noted, and will be fitted into next steps for Stakeholder Group discussions of other possible strategies.

Urgent Strategy #6: Restructure Business Tax to Modernize and Reflect Current Business Profile

Presenter: Paul Krutko, Chief Development Officer, Office of Economic Development (<http://www.sanjoseca.gov/StakeholderGroup08.asp>). May 5 (Slides 8-15)

Management Partners Report Revenue Strategy #4 pp 68. Strategy was presented with 2 options: A. Modernize Business Tax rates by indexing rates to current CPI and raising maximums, and B-1, B-2. Restructure Business Tax Formula, including card rooms and not including card rooms.

STRATEGY		6: Restructure Business Tax to Modernize and Reflect Current Business Profile		
	ADVANTAGES			CONCERNS
1.	CPI adjustments are predictable, consistent and understandable		1.	Increasing/doubling business tax in a down economy
			2.	Potentially regressive nature of across the board increase
			3.	High cost of doing business in San José
			4.	Current business tax is higher than that in nearby cities
			5.	Instant doubling of fees: phase in over time?
			6.	Gross receipts difficult to administer and penalizes successful businesses
			7.	Will make it easier for cities in other states to get San José businesses to locate elsewhere
			8.	If card room tax increase, some of it should go to gambling services
			9.	Will we lose revenue if very small businesses just don't pay the tax?
			10.	Businesses tax model generates declining revenues; property tax percent for business is much less than residential since Prop 13.
			11.	In isolation, without other considerations like fewer regulatory burdens, raising taxes is not attractive
			12.	Don't have information from City regarding where do businesses go if they don't renew their licenses

Stakeholder Question: How many businesses operate under CUP or have to have extra permits, such as BID?

Some concern was expressed that previous measures to increase failed voter approval in a good economy. Now with a bad economy, we are asking that the tax double and to increase the sales tax. Business tax was equalized for surrounding cities into a per capita number and provided: San Jose \$25.92 per capita; Fremont \$34.70 per capita; Sunnyvale \$8.21 per capita; Santa Clara \$7.52 per capita; Mountain View \$3.88 per capita. Several other cities do not have business tax. Reason for "per capita" measure is to get a comparable comparison to measure across several strategies as a way to benchmark. Some expresses concern with per capita basis; would be more interested in what businesses are actually paying.

Stakeholder member has a detailed analysis of business comparisons in area. Will email analysis to Pete.Constant@sanjoseca.gov and made available to group. Another Stakeholder member expressed that if we increase “sin tax,” then some of the revenue received should be put back into economy for services that support those “sins.”

Stakeholder Question: Do we have dollars of small sole proprietorships versus \$1M+ companies? Finance Department database is 85,000 entities, based on self-reporting employment numbers. A report to categorize could be made available. Category suggested was 1-less than 10 employees, over 25 but less than 100, compared to peer group. Economic Development thinks categories of 10 to 100 employees is more indicative. Additional information provided that out of 85,000 entities, 30,000 were classified as “exempt” – not enough receipts or hardship category.

Stakeholder Question: How do other cities treat increases to business tax – Austin, Raleigh, Scottsdale, Tempe AZ, Denver? These are places where San José companies have moved.

Urgent Strategy #8: Increase Revenues from Visitors who benefit from General Fund Services

Presenter: Ed Shikada, Deputy City Manager

(<http://www.sanjoseca.gov/StakeholderGroup08.asp>) May 5 (Slides 16-22).

Management Partners Report Revenue Strategy #86 pp 78. Strategy was presented in 3 parts: 1. Increase Transient Occupancy Tax and shift to General Fund; 2. Establish Parking Tax on City/RDA-owned parking lots or all parking lots; and 3. Establish a Vehicle Rental Tax.

STRATEGY		8: Increase Revenues from Visitors who benefit from General Fund Services		
	ADVANTAGES			CONCERNS
1.	Many cities impose vehicle rental taxes and we should return the favor		1.	A state pre-emption of vehicle rental taxes
2.	Vehicle rental tax a good proxy for TOT increase		2.	Impact on downtown
			3.	Effect on visitors versus residents
			4.	Number of hotels serving San José are actually in neighboring cities and might have lower TOT, free parking
			5.	Other city comparisons

Clarification on Slide #20 item A: of the potential annual revenue of \$5.1 Million, breakdown is:

Airport \$3.6 M

Downtown Dept of Transportation lots \$900 K

HP Pavilion \$300 K Downtown RDA lots \$200 K

Regional Parks \$100 K

Stakeholder Question: Could this be a rate increase and not a tax? Can be a rate increase on all non-Airport lots in order to benefit General Fund, but would also have to follow existing formulas for distribution. A rate increase at Airport needs to go back to Airport. A general tax

would be assessed citywide and goes directly to General Fund revenues, with no restrictions on use.

Hotels are raising a “Hotel Taxing District” which would essentially raise a tax similar to TOT and it would be dedicated to Convention Center expansion. City not recommending an increase to TOT at this time, so as not to double the increase.

Urgent Strategy #10: Modernize Utility Users Tax (UUT) and Consider Increase to Bring into Alignment with Other Large Cities

Presenter Scott Johnson, Director, Finance Department

(<http://www.sanjoseca.gov/StakeholderGroup08.asp>) May 5 (Slides 23-29).

Management Partners Report Revenue Strategy #5 pp 71. Strategy was presented with 2 options:

A. Increase Utility Users Tax citywide; and B. Maintain the current tax rate and modernize telephone users tax.

STRATEGY		10: Modernize Utility Users Tax (UUT) and Consider Increase to Bring into Alignment with Other Large Cities		
	ADVANTAGES			CONCERNS
1.	UUT shares burden of paying for services very broadly		1.	Local peer cities have lower rate than San José
2.	Modernization creates more equity		2.	Interim option B – goes to voter, then in 2 years, increase/restructure = 2 ballot measures in 3 years
3.	Addresses future innovations, more flexible		3.	Regressive – hit low income residents harder

Stakeholder Question: What is UUT distribution of cities around San José?

Sunnyvale 2% Mountain View 3%

Oakland, Los Angeles, San Diego, Long Beach 6.83%

Milpitas, Fresno no tax Santa Clara has own utility as major revenue source

Stakeholder Question: Do we tax cable? No, but we collect a Franchise Fee. But with bundled services, we have a revenue stream gap.

Stakeholder Question: What is the impact of the City’s “green vision” which promotes reduction of energy usage by 50%? Would the drop in revenues be offset by projected growth of 350,000 in population in next 25 years?

Stakeholder Group added one additional strategy for consideration on a November 2008 ballot: Increase Number of Card Room Tables Allowed in San José. According to City Attorney, an increase in tables would require voter approval. There was no prepared presentation.

STRATEGY		Increase Number of Card Room Tables Allowed			
	ADVANTAGES			CONCERNS	
1.	Residents are going out of area to gamble because not enough tables		1.	Targeting a particular population	
2.	More give & take: Could give more tables and take in higher tax rate – increase revenue to San José (package)		2.	Offset public benefit of increased revenues with greater problems from gambling – require more intervention services at greater cost	
3.	Approximately up to \$6 Million per Business Journal. (Dollars contrast with current annual revenue of approx. \$11.2 Million)		3.	Crimes associated with card rooms, workload on Police Department regarding background checks and licensing card room employees	
			4.	Cost/benefit – how to recover costs	

Stakeholder Question: Referencing article in 4/11/08 Business Journal, policies made by City Council in the past should be reviewed.

Clarification: City is currently in litigation with one card room.

Strategy Preferences Exercise

Originally the Stakeholder Group was requested to select 3 strategies they preferred to go forward for consideration on the November 2008 ballot (green dots), and one strategy they definitely could not support (red dot). Several objections were expressed about the limitations of only being able to comment on 4 out of the 11 strategies, some with multiple options. It was determined that the Landscape and Lighting District strategy (presented on 4/28/08, Urgent Strategy #5) and the Card Room Table Increase be added to the preferred ranking list. It was also determined that a better representation of the preferences of the Stakeholder Group would provide a rating on each strategy and option as follows:

- A YES indicated that the Group preferred this tax go forward for consideration by the City Manager for a November 2008 ballot.
- A NO indicated that the Group members did not support this type of tax measure.
- A KA (Keep Alive) indicated that the tax strategy was worth considering, but more information and discussions were needed before a definitive preference could be provided.

The results on the strategy options are attached.

The advisory results of these preference indicators will be sent to the City Manager for use in her report to the City Council in preparation for the MBA due out this week and in the final Elimination Plan to be presented to Council in November 2008.

HONORABLE MAYOR AND CITY COUNCIL

May 9, 2008

Subject: Three-Year Structural Budget Deficit Elimination Plan-Top Priority Strategies

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Closing: Next meeting will take place on June 2, 2008 at City Hall, Wing Rooms 118-120. The discussion will include new strategy suggestions from the Stakeholder Group to be grouped with the Management Partners remaining Top Priority Strategies. If a theme can be determined for grouping these strategies, staff analyses and presentations will be brought to the group at the June/July scheduled meetings. These new strategy suggestions will include the Working Partnerships report and the Neighborhood Associations reports. These and additional suggestions can be emailed prior to the June 2 meeting to Pete.Constant@sanjoseca.gov, or to District1@sanjoseca.gov

Public Comment: None

Meeting was adjourned at 9:12 pm.

Description of Urgent Strategy for Potential Placement on November 2008 Ballot	Support	Oppose	Want More Info
(6A) Modernize Business Tax rates by indexing rates to current Consumer Price Index (CPI) and raising maximums <i>(voter approval)</i>	↑↑↑↑↑ 5	↓↓↓↓↓ ↓↓↓↓↓ ↓ 11	→→→→→ →→→→→ → 11
(6B-1) Restructure Business Tax Formula (including cardrooms) <i>(voter approval)</i>	0	↓↓↓↓↓ ↓↓↓↓↓ ↓↓ 12	→→→→→ →→ 7
(6B-2) Restructure Business Tax Formula (non-cardroom) <i>(voter approval)</i>	0	↓↓↓↓↓ ↓↓↓↓↓ ↓↓↓↓↓ 15	→→→→→ →→ 7
(7A) Increase Construction/Conveyance Tax; allow more Parks Maintenance and potentially other uses <i>(voter approval)</i>	↑↑↑↑↑ ↑↑↑↑↑ ↑↑ 12	↓↓↓↓↓ 5	→→ 2
(7B) No increase to Construction/Conveyance Tax; allow more Parks Maintenance	↑↑↑↑↑ ↑↑↑↑↑ ↑ 11	↓↓↓↓↓ 4	→→→→→ 5
(7C) No increase to Construction/Conveyance Tax; shift all revenues to General Fund	0	↓↓↓↓↓ ↓↓↓↓↓ ↓↓↓↓↓ ↓↓↓ 18	0
(7D) No increase to Construction/Conveyance Tax; shift non-Parks allocations only	0	↓↓↓↓↓ ↓↓↓↓↓ ↓↓↓↓↓ ↓↓ 17	→ 1
(8-1) Increase Transient Occupancy Tax (TOT) to Market and shift to General Fund (not recommended) <i>(voter approval)</i>	↑↑↑ 3	↓↓↓↓↓ ↓↓↓↓↓ ↓↓ 12	→→→→→ →→→→→ 9

(8-2) Establish a Parking tax (on City/RDA owned or all parking lots) (voter approval)	↑↑↑↑↑ ↑↑↑ 8	↓↓↓↓↓ ↓↓↓↓↓ ↓ 11	→→→→→ 4
(8-3) Establish Vehicle Rental Tax (voter approval)	↑↑↑↑↑ ↑↑↑↑↑ ↑↑↑↑↑ ↑↑ 17	↓↓ 2	→→→→→→→→ →→→→→→→→ →→ 11
(9) Increase Sales Tax to provide increased General Fund revenues (voter approval)	0	↓↓↓↓↓ ↓↓↓↓↓ ↓↓↓↓↓ 15	→→→→→→→→ →→ 6
(10A) Increase Citywide Utility Users Tax (UUT) (voter approval)	0	↓↓↓↓↓ ↓↓↓↓↓ ↓↓↓↓↓ 14	→→→→→→→→ →→→→→ 8
(10B) Maintain current UUT and modernize Telephone Users Tax (voter approval)	↑↑↑↑↑ ↑↑↑↑↑ ↑↑↑↑↑ ↑↑ 17	↓↓ 2	0
NEW: Card Rooms-Increase rate to 15% (tax only)	↑↑↑↑↑ ↑↑ 7	↓ 1	→→→→→→→→ →→→→→→→→ →→ 11
NEW: Card Rooms-Increase rate to 15% with increase in # of tables	↑↑↑↑↑ ↑↑↑↑↑ 10	↓↓ 2	→→→→→→→→ →→→→→→→→ 10
PRIOR DISCUSSION: Lighting/Landscape District Citywide	N/A	N/A	→→→→→→→→ →→→→→→→→ →→→→→→→→ →→→→→→→→ 20